

The regulation of local public services in the EU and the Italian case

Andrea Sbandati
International Summer School in Applied
Environmental and Regulatory Economics
Torino, September 2010

1

Local public services: a definition

- Local public services are the services provided on local (not national or international) base.
- There are many local services, regulated in different ways in every State.
- The European Union does not use the term “local public services”, but the more generic “services of general interest”.
- In this lesson we consider the following local services: water and wastewater services and urban waste management.

2

Lecture summary

1. Regulation of local public services in Europe:
 - a) The legal European framework
 - b) Regulation in the main Countries
 - c) Companies and main operators
2. The Italian case
 - a) The Italian law on local public services
 - b) Regulation on “integrated water service”
 - c) Regulation on “urban waste management”
3. Conclusions

3

Some rewards

- Local public services (specific focus on water and waste services) are provided in different ways in different countries.
- They depend on EU laws and principles, on national, regional and local laws and regulations.
- They are influenced by culture, history, and politics background of different countries in different periods.
- It's difficult to have updated and analytics information on these sectors in the different countries.
- This is the reason why this lesson needs to be “generic”, I apologize.

4

The EU legal framework

- The European level of regulation on these sectors is more and more important in the late years, due to the activities of European Commission, and European Court of Justice.
- Concerning regulation on water services and urban waste management, there are no specific European Directives (the existing sector called Directives regulates technical and environmental aspects, etc.);
- No “liberalization Directive” has never been approved on these sectors (like happened in energy, transports and communications services).
- Anyway the organization of these services in every single country must respect the “European general principles” and the directives on public contracts.
- Concerning services of general interest, the European Commission promoted several “discussion paper” (white paper and green paper), regarding the whole sector, the problems of “concessions”, the use of Public Private Partnership.
- Important statements are included in the European Treaty, and the European Court of Justice, on these bases, has published many important decisions (especially about in house contracts cases in single States).

5

The EU legal framework

- In this regards, we need to analyze:
 - The new Treaty on the Functioning of the European Union
 - The Directive on public sector
 - The Commission Communication on services of general interest
 - The Commission Communications on concessions
 - The Commission Communications on public private partnership
 - The European Court of Justice decisions on local services
- You have already received documents about these topics.

6

European Treaty and the general principles

- The European Treaty (art. 49¹ TFEU and following) underline the importance of economic competition, and the freedom of circulation of goods, people, money and services. These articles are the base of the “competition philosophy” in local services policies.
- The European Treaty (art. 14² TFEU and 106³ TFEU), at the same time, describes “services of general interest” like special activities; these are important for the economic development and social cohesion, and could not be subjected to “competition principles”. These articles are the base of the “non-competition philosophy” in local services policies.

1 Previously Art. 43 and following TCE

2 Previously Art. 16 TCE

3 Previously Art. 86 TCE

The public contracts Directive

- In order to promote the competition and the open European market, EU approved a “Directive on public contracts”.
- Following the Directive, every public administration in EU must chose a supplier for a public contract (even for services) only by tender. The tender’s procedure must respect “the transparency and non-discrimination principles” of the Treaty.
- Then, when a “local public service” is a “public contract”, the public administrations must use a competitive tender, open to the participation of all the operators on European scale.
- The Directive include some “exceptions”.

The problem of “concessions”

- The Public Contract Directive must be used by the Member States, only in case of “contracts” (when the public administration directly gives some money to an operator for a specific service).
- In case of concession, the rule is different: the public administration chooses an operator for a public service (like water service), but the operator is directly paid by consumers, without direct transfer of money from the public administration to the operator
- The Public Contract Directive must be used for “contracts”, not for “concessions”.
- Many Local Public Services are organized like concessions, so a problem rises.
- In fact, there is no European Law about Concessions, as the European Commission itself said.

9

The Communication on “concessions”

- In order to better clarify this issue, the European Commission published two different “Interpretative communication on concessions”.
- In these documents the Commission explains that there is no specific European regulation on concessions and that, in case of concession, it is not necessary to follow the procedures provided by the Public Contract Directive (competitive tender).
- At the same time the Interpretative communications underline that, in case of “concessions”, it must be respected the “Treaty principles” about competition and competitive market (included transparency and non discrimination principles).
- So, in case of Concessions, Member States can adopt a more flexible legislation on public services providing, including competitive procedures, not only “tender”.

10

A special procedure: public-private partnership (PPP)

- In many Member States public services (even waste and water services) are provided by the establishment of a mixed ownership enterprise, between the local administration and one or more private companies.
- The European Commission then decided to have a report on this specific form to manage local public service (Green Paper) analyzing the “public private partnership” experiences in different countries.
- The report describes different forms of PPPs and tries to value the compatibility of PPPs with the European principles about competition and open market and about the public contract legislation.
- The paper underlines that the PPPs procedures can't avoid the competition procedures in providing public local services, defined in the public contract directive and in the general competition Treaty principles.

11

The Interpretative Communication on PPP

- After the Green Paper, European Commission adopted a “Interpretative Communications on PPPs”, in the 2009.
- In this document the Commission states that PPPs are compatible with the European laws and principles on competition, only if the private partner has been selected through a competitive procedure, which respects the transparency and non-discrimination principles.
- The Communication states that, when the tender for choosing a private partner is done, it is not necessary to do the tender for concession. This is a very important statement, which clarifies a complex legal problem faced from every Member States.
- The Communication also defines specific procedures that need to be followed in the tender for the private partner, underlining that the object of the tender is the quality and quantity of the services provided by the mixed ownership company and the prices (the private selection must not be a only-financial operation).

12

Companies listed in the Stock Exchange

- Many operators (the biggest) providing public local services in Europe are companies listed in the Stock Exchange.
- In some cases they provide services after a tender for the contract or the concession, following the public contract directive or the general principles on concessions.
- In similar cases (like the water service in England and Wales) they provide public service without any tenders. They are regulated by a national authority, and the competition is guaranteed by the permanent possibility of take-over by other operator, in the Market.
- The Interpretative Communication doesn't explain if the procedure of listing in the Stock Exchange could be considered a competitive procedure to select one or more private partners.
- This point needs to be clarified in the future.

13

Not competition: the “in house” possibility

- In Europe, in many cases, local public services are provided by public companies owned by the local administration.
- Usually these companies (or sometimes special economics bodies not created in the form of company) provide services thanks to a “direct contract” with the local administration, without any tenders or competitive procedures.
- European Commission and European Court of Justice examined these cases, considered incompatible with the Public Contract Directive (if a public contract) and with the general competition principles (in case of concession).
- At the same time Member States and local communities considered “direct contracts” to public companies owned by themselves, absolutely legal.
- Tender, for them, is compulsory when a local administration chooses an operator “in the market”. But it is always possible for an administration to provide a service directly, without using the market.

14

The “in house” decisions of the Court of Justice

- In order to solve this discussion the Court of Justice has adopted many decisions, using the term “in house providing”.
- The Court stated the conditions to be followed for an “in house” providing contract.
- For the Court a direct contract with a public company could be considered “legal” if the local authority exercises over the company a control which is similar to that they exercise over their own departments and, at the same time, the enterprise must carry out the essential part of its activities with the controlling authorities.
- The Court stated also that in case of “in house” contract, the company must be entirely owned by one or more public authorities, and any private body can be a shareholder.
- Following these conditions “direct contract” with public companies are “legal” for the Court, being considered the only “exception” to the competition rules in the European market.
- Not every public companies with “direct contract” without tender respect the “in house standard” defined by the Court.

15

Legal and illegal procedures

<i>Legal procedures</i>	<i>Illegal procedures</i>	<i>Not clear procedures</i>
Tender for contract or concession	Concessions or contracts without tender	Companies listed in Stock Exchange
PPP with tender for the private partner	PPP without tender for the private partners	
Public companies respecting the "in house" standard	Public companies not respecting the "in house" standard	

16

Economic regulation problems in the main countries

- Regulation problems in public local services providing don't concern only the legal framework.
- The economic regulation (tariffs, contracts, efficiency, investments) is defined by the single Member States, for every single service, in different ways.
- There is any "European standard" in the economic regulations of local public services (no law, directive and regulation).
- We analyze the most important "patterns" of regulation used by the different countries.

17

Economic regulation problems

- Waste and water services are local, natural and legal, monopolies, in all the European countries (waste collection is liberalized in some regions of Finland).
- In spite of it, economic regulation in local public service usually is not strong in Europe.
- There are few real "national authorities" (England, Wales, Portugal). Sometimes there are national or regional "offices" with some regulation or information duties and skills.
- Tariffs, efficiency and investments are often not regulated by national laws, but directly by the local authorities. In the case of waste services often there are no "tariffs", but taxes.
- Economic efficiency is weakly regulated: in case of tender (concessions, PPP) through the competition, in case of in house providing through the control (sometimes) of the local authorities like owners.
- The England and Wales "model" in water services is unique, with private operators listed in Stock Exchange regulated by a national authority (Ofwat).

18

Providing procedures and economic regulation

<i>Providing procedure</i>	<i>Economic regulation</i>	<i>Where</i>
Tender for contract or concession	Tender , tariff regulation, contract, authority	Germany, France, Eastern Europe countries
PPP	Tender for private partner , tariff regulation, contract, authority	Italy, Germany, France
In house	Tariff regulation, contract, authority	Italy, Germany, France
Companies listed in Stock Exchange	Tariff regulation, contract , take over, authority	England, Wales

19

Companies and main operators

- On the supply side the local services market is highly scattered:
 - Some local authorities (often the smallest ones) provide directly the services. These are no market activities.
 - Many local authorities provide the service through their own companies or special statutory enterprise (*stadtwerke, municipalizzate*). The dimension of the company depends on the dimension of the municipality. Usually these are “in house” companies, the market activity is weak.
 - Some local authorities provide the service through mixed ownership enterprises (PPPs). Sometimes these are market-oriented companies, sometimes a sort of “in house” companies.
 - Many private operators provide local services, usually having won a tender or being regulated by authorities (UK). The largest companies are fully market oriented companies. Many small private and cooperatives companies operates in these sectors, usually on local and regional base.

20

The Italian case – the legal framework

- The Italian legal framework in the field of local services of general interest is complex and continuously changing.
- We must consider:
 - National “horizontal legislation” (local government act);
 - Sectorial national laws (energy, water, waste, transportation);
 - Regional general and sectorial laws (Constitutional Reform in 2001)

21

Local Government Act

- The rules about contracting out of local services of general interest in Italy are included in the National Local Government Act (Testo Unico Enti Locali, **art. 113**). The law was issued in 2000 and amended in 2003.
- According to the law Municipalities have three “legal” possibilities for contracting out local services :
 - The franchise bidding (FB) –
 - The establishment of a mixed ownership enterprise (MOE) in which the private partner has to be selected through competitive bidding procedures, assuring the complete and rigorous respect of national and European legislation;
 - The establishment of a completely public enterprise, on whom local authorities exercise a control which is similar to the one they have over their own department, and, at the same time, the enterprise must carry out the essential part of its activities with controlling authorities (in house providing – IHP)
- The companies listed on the Stock Exchange before October 2003 are considered “legal”.
- All other contracts are considered “illegal” and must be cancelled within 2010 (concessions without tender, mixed company without tender for the partner, all-public company without “in house” standard providing).

22

Sectorial legislation

- Sectorial legislation (water and waste) has reduced municipalities freedom of choice, in order of contracting out local services of general interest.
- Also for the municipal solid waste management, municipalities are now obliged to tender the service (Environmental legislation, issued in 2006).

23

Contracting out possibilities by sector

Sector	Forms of contracting out	Years of concession	Suppliers/Regulator
Electricity (distribution)	Concession to ENEL	35	National Government/Energy Authority
Gas (distribution)	Franchise bidding	Max 12	Single Municipalities/Energy Authority
Water service	Franchise bidding Mixed ownership enterprise with tender for the private partner In house	Max 30	“Ambiti Territoriali Ottimali” (many municipalities)/no national Authority
Municipal solid waste management	Franchise bidding Mixed ownership enterprise with tender for the private partner In house	Min 15	“Ambiti Territoriali Ottimali” (many municipalities)/no national Authority
Local public transportation	Franchise bidding	5	Regions – Provinces – Municipalities. No national Authority ²⁴

Changing legislation

- Main issues to discuss:
 - Strong restriction of “in house” providing and of mixed ownership enterprise. Municipalities could use these possibilities only in “special market condition” (lack of competition). Franchise bidding is considered the “main street”;
 - Special regulation only for water services (widen the role of public in water management).;
 - Reorganization of local Agencies (waste management regulating and programming activities could be transferred from Municipalities to Provinces)
 - Reorganization of National Agencies (including waste and water sectors)

25

Companies and municipalities

- In Italy the most of enterprises which manage local services of general interest are owned by municipalities.
- Relationships between local authority (often Municipalities) and companies are regulated by contracts (service contracts).
- The single municipality is at the same time “local regulator” and “shareholder”.
- Is there a “conflict of interest” between “regulator” and “the regulated” ? How can we solve this problem ?
- The problem involves not only the “in house providing” enterprises, but also “mixed ownership enterprises” and companies listed on the stock exchange.
- The problem is particularly strong in water-, waste- and transportation sector, where there not National Agencies, and the Municipalities are the only “regulators”.

26

Conflict of interest: an example



27

Governance problems - 1

- In Italy, almost all public enterprises managing local service of general interest are joint stock companies; some of them are listed in the Stock Exchange.
- “Special statutory enterprises” (“aziende municipalizzate/speciali”), are almost all transformed in joint stock companies, in the late years.
- Governance of joint stock companies is regulated by the commercial law (Civil Code - Codice Civile).
- In the case of companies owned by municipalities it must be considered also the Local Government legislation: a matter of complexity.

28

Public companies and markets

Sector	% of market managed by public companies
Gas	50
Water	90
Waste	60
Transports	100

29

Stock companies and markets

Sector	% stock companies on total public companies
Gas	100 %
Water	90 %
Waste	80 %
Transports	80 %

30

Governance problems – 2

- Usually, Italian public companies managing local services of general interest use a “traditional form of Governance”, based on:
 - General Meeting of Shareholders
 - Board of Directors (BOD)
 - Executive committee (not often)
 - President and/or Managing Director
 - Board of Auditors
- Very few companies use the “dualistic system”.

31

Governance problems - 3

- General Meeting of Shareholders is formed by the Mayors of municipalities, owners of the company.
- Directors are named by the General Meeting of Shareholders, which decides in order to the number of the components of the Board and their remuneration.
- Directors are designed directly by the Mayor, by a personal decree.
- Board of Directors is an “independent body” in managing the company. Directors cannot be revoked by the General Meeting of Shareholders (the term of office is three years).
- General Meeting of Shareholders approves (or does not) the balance of the company (seldom the budget). Sometimes the shareholders approve “strategic documents” for the companies, which directors must respect in managing the company.
- Internal account control is guaranteed by the Board of Auditors, named by the General Meeting of Shareholders, among independent personalities.

32

Governance problems - 4

- Municipality Council do not participate in the management of the company.
- Municipality Council decides only on the creation of new companies, on possible mergers, and liquidation.
- Municipalities are obliged by law to organize a specific office for monitoring the municipally owned companies (balance analysis, benchmarking, contracts control).

33

Governance problems - 5

- Mayors and assessors cannot be named in the boards of the companies (incompatibility).
- Conflict of interest is regulated by the commercial law (Civil code).
- In the case of companies listed in the Stock Exchange, shareholders must respect a specific self-regulation code (the so called *Pređa code*) in naming directors.

34

Governance problems - 6

- In the case of companies owned by several municipalities, relationships between public shareholders are regulated by specific “shareholders agreements”. These agreements regulate:
 - Methods for naming the BOD, the CEO, the Company President, and the Board of Auditors;
 - The smaller shareholders’ rights.
- The Statute of the company defines the General meeting of shareholders majority to approve the balance and other extraordinary decisions (e.g. liquidation, etc.).

35

Governance problems – 7

- In case of mixed ownership enterprises, relationships between public and private shareholders are regulated by “special agreements” which define:
 - The method for naming the BOD, the CEO, the Company President, and the Board of Auditors.
 - Usually the President is designed by public shareholders, and the CEO by the private ones.
 - The shareholders rights;
 - The possibility to pass from majority public company to minority public company.
- The Statute of the company defines the general meeting majority to approve the balance and other extraordinary decisions (e.g. liquidation, etc.).

36

Governance problems - 8

- In the case of “in house providing”, the municipality (or municipalities) must *exercise over the company a control which is similar to that they exercise over their own departments and, at the same time, the enterprise must carry out the essential part of its activities with the controlling authorities.*
- Since most of the Italian companies are “joint stock companies”, it’s very difficult to observe such “in house standards”.
- According to the Italian Commercial law (Civil code) the Board of Director is an independent body from shareholders in managing the company. Shareholders cannot interfere directly in managing operations of the company.
- Contracts between Municipalities and companies are often based on “standard contracts”, issued by Governments or Regions. They can’t be changed easily.

37

Future restrictions to public companies

- Italian legislation in the next year could restrict the possibility for Municipalities to operate through owned companies in many fields (Budget law 2007).
- Stock companies owned by local administrations (Regions, Provinces, Municipalities) can work (have contracts only) for the public owner (they cannot run market activities, and are obliged to sell “private” contracts by 2007).
- Municipalities cannot have direct contracts with their owned companies (public or mixed), for different activities than “local services of general interest” (e.g.: software, tax collecting, maintenance, etc.).

38